

9/4/97 Notes - RSFA Meeting with Industry on Lessee/Designee Issue

Attendees: MMS - Don Sant, Ken Vogel, Vern Ingraham, Boh Walker, Larry Gratz, Barbara Lynham, Jan Therkildsen

Industry - Dennis Pade and Chris Pennels, TTTI; George Pritchard, Texaco E&P; Scott Dean, Texaco, Inc.; Don Lynch and Ken Wells, Texaco Offshore; Wayne Paschall, Texaco; Carla Wilson, IPAMS; George Butler, Chevron; Nina Thornton, Fina; John Clark, Conoco; Bill Strain, Chevron; Bob Wilkinson, Amoco; and Patsy Bragg, Gardner & Wynne

Time & Location: RMOGA, 1775 Sherman, 9:30 - 3:00 pm

Meeting Objective (as stated by Patsy Bragg): To sort out what Industry and MMS have learned and to talk about the long term objective of the lessee/designee issue.

Preliminary discussion: George Butler - Comment Period for Interim Final Rule ends 10/6/97. What implication does that have for MMS on their ability to comment during the pendency of the comment period?

Don Sant and Ken Vogel said they anticipated a 2-way dialogue at this meeting and that the pendency of the comment period didn't create a problem for them in commenting.

Order of Meeting Notes:

Page 1 Dear Payor Letter Responses So Far

2 Status of Followup Letters to Designee (to verify someone is paying on their behalf)

2 Designation Form

3 Database

4 Exception Basis

5 Interim Final Rule

6 Stranger Payments

7 August 14 Dear Payor Letter

7 Takes vs. Entitlements

8 Lessee of Record AND Operating Rights Designations

8 Process in the Future

Att. Process Flow Diagram

Att. Texaco Trading Designation form

Att. Draft Designation Form

Dear Payor Letter Responses So Far

Larry Gratz reported: Respondents: 2645 potential respondents (payors in MMS database)
(158) indicated they were no longer payors
2487 actual potential respondents
1050 replies (roughly 40-42%); 750 loaded into database
Of the top 10 payors by \$\$, 5 responded and 5 have not.

Leases: 125K records to start with (69K still blank)
dbase has expanded to 185K records (each
designation creates a record)
260K is the potentially expected amount of records
44% complete (Larry's approximate guess)
18K leases have some info; on 5K leases, payor is lessee;
13K involve designations

Larry reported that many responses are incomplete or incorrect: missing TIN (especially for lessee), missing address, incorrect name ("Bill"), etc.

Status of Followup Letters to Designee (to verify someone is paying on their behalf)

George B. - The commitment was that MMS would use the information to turn around and go to names and addresses. We didn't understand that MMS should "shut down" until they received 90% of the data.

Ken V. - We wanted to consolidate the information before we went for designations; it was an attempt to not be overly burdensome. Now that we have the Interim Final rule and have satisfied the Paperwork Reduction Act requirements, we're going to do a test of 10 letters to see if we can get feedback on what people do know/don't know.

Larry G. - It is our intent to consolidate the information before we go to the lessees. However, we're having trouble extracting the information in a consolidated basis from the database.

Don S. - MMS will wait until after the 60 days mentioned in the August 14 D.P. letter to send.

John C. - I want the ability to say you're not right that I'm paying on your behalf. I don't know who's saying I'm paying on their behalf.

Ken W. - When January letter went out, we complied (Texaco offshore). Some companies were not willing to give us TIN #'s. Legal advisors told us to go out with our own followup letters saying that we have told MMS we are paying on your behalf and asking for written designations. 50% have responded.

Dennis Pade and Chris Pennels of TTTI said they had followed the same process with 75% response (copy their designation form is attached).

Designation Form

Don Sant shared the draft version of the form (attached) MMS proposes to have lessees use to submit to MMS. The form includes data elements MMS needs.

Ken V. - We are hoping as much of this can be done electronically as possible. We do not want 250,000 of these forms. We are looking at KIOSK's etc. We believe we have the obligation to educate lessees on their new responsibilities.

Don S. - If you have reactions or suggestions, let us know. We can make changes before we go to OMB for approval of the form.

Database

George Butler: FOGDMA & RSFA don't confer the right to MMS to build a database.

Don S. - What is the database issue?

Bob W. - Information is obsolete the day after it is sent in, so I have a problem with sending all this information up-front. Amoco does not have a problem helping you determine them when there is a problem collecting on a specific property.

- Ken V. - As long as we KNOW you're going to pay, no problem. You could decide NOT to pay any more.

Patsy B. - No problem so far. What's the basis for determining there will be a problem?

- Ken V. - Fact that it hasn't happened does not mean won't happen next month. Problem is theoretical. MMS has no firm ideas on how to maintain database; we do not want to make more work for you or for us. The database will be used to allow us to give notifications to proper parties under RSFA when we send out demands. Very few demands related to production after 9/96 have been sent. We began sending bills without demand language attached to them (principally interest bills). Payors have mostly assumed responsibility to pay.
- Don S. - Your (Patsy) concerns are also theoretical. We haven't said we're going out with a mass request to payors. We're concerned that we have information when the payor is not the lessee so we can issue an order.

Patsy Bragg - The issue is should MMS be building the database or should you go to BLM or Offshore.

Ken V. - They don't have information on who asked Chevron to pay.

George B. - I'm concerned that in the future there will be PIF/designee comparisons (like AFS/PAAS) that we might start doing.

Ken V. - That approach is under consideration.

Bill Strain - Took us 5-8 weeks to reply. Probably what we provided is stale. How are we going to be required to refresh.

John Clark - I don't care what you do with the database. My concern is there was never agreement on keeping it updated.

Don S. - We are hoping we can keep updates through getting designation form. We have not decided how to maintain a database. We will scan designations, enter them into a database, and eventually make available electronic capability.

Patsy Bragg - Considering the order of magnitude, what quality of information will satisfy MMS's needs?

Don Sant - We're not going to do much verification work except on larger producing leases.

Patsy Bragg - Do you expect lessees to file different designations every month?

Ken V. - If a lessee sells to 3 payors (different ones different months), they could designate all 3 and be fine. Overlapping start and end dates are no problem. Only need to change when no longer involved with a property or when a change is long-term.

Exception Basis

Industry participants wanted to discuss complying with RSFA on an exception basis.

- **Bob W. -** If demands are very infrequent, why wouldn't you consider exception basis? Information is available with BLM to get lessee information and address.
- **Patsy B. -** Why wouldn't audit mechanism satisfy in less burdensome way? Automated bills, collection process generates only 300 per year that need followup? You have a relatively small set. You have 6-7 years left in the statute of limitations. You don't send demands to ALL lessees; only to a small portion. Industry is getting the brunt when it's really the Federal Government that hasn't been maintaining the proper data.
- **Carla W. -** Why can't you wait until you have a finding and then ask for the lessee information.

MMS Responses:

- **Don S. -** We have found through the January Dear Payor process that the data is not readily available for even the current time periods. We heard over here that Texaco is having trouble gathering information on who they are paying for on 100% of their leases for September of 1996. If they don't know that today, certainly they're not going to know it 5 years from now (during audit). Education is needed to make sure payors know that data needs to be somewhere.
- **Ken V. -** Statute requires designation has to be in writing FROM the designator (lessee/ operating rights owner). Audit process won't help if payor says someone is responsible and they haven't designated and won't accept responsibility. If we knowingly don't provide for a way for lessees to comply with the law, we will be subject to criticism. We realize it's not ideal. We are trying to make the easiest system possible for lessees to comply with the law.
- **Ken V. -** Lessees are missing information on how well goes with AID number.
- **Don S. -** That's why we followed the process this group agreed to last fall.
- **Ken V. -** In the past process. We only do followup when a bill is ignored. Remember, pre-appeal we're supposed to send a notice to all lessees. But if a bill is appealed, we must send out a demand and notice to lessees.
- **Ken V. -** So far on average it has taken us 1 month per lease to get information back from BLM (BLM says it takes them from 6 to 40 hours per lease to do the research). Clearly it's not worth BLM's time for a bill of \$1,000. We're supposed to be cost effective. If we have NO information, the threshold will be higher on what we will do to collect than if we have the information. Payors will figure out that they don't need to pay small bills.
- **Don S. -** If we went back to the BLM adjudication process, it would be more costly to industry than this approach.
- **Ken V. -** Neither MMS Offshore or BLM has complete information on owners. There are a lot of owners who think that filing in local courthouse is all they need to do. BLM

doesn't approve working interest ownership transfers now. Even if the data was good, it would NOT satisfy RSFA (written designations). It would not provide the tie. We COULD use one form at the time they file ownership transfer (either to MMS or BLM -- one form).

- Don S. - We have received answers people don't know; especially for older time periods. That's why without a good education process up-front we can't do it on an exception basis. Ignorance is costly to MMS if people can't tell us down the road who was liable (per RSFA).
 - Ken Vogel - As the process gets going, there will be several hundred per month for which we send demands (because of no compliance with bills or because of appeals).
- George Butler - If lessees would just do their designations, MMS would be protected.
Don S. - And link between lessee and particular payor.

Interim Final Rule

Don Sant encouraged industry to file their comments on the rule.

George Butler asked that his comments on the Interim Final rule be entered into the record of this meeting. He will also submit written comments. His comments included:

- There were problems with Payor Liability. MMS could come after anyone involved (too joint and several for us) Fairness places legal obligation/liability on lessee to pay in accordance with MMS rules. Gives options to have some pay on behalf. Fairness imposes on lessee and lessee ONLY.
- This rule goes beyond what I think you have the legal right to do. You don't have to show good cause. It is so broadly worded, it purports to place a burden on payors to provide information to MMS at your whim.

Don S. - I hope we can use the designation form when we need information. But if it doesn't work, we need the right to ask the payor.

- Chevron contends that a rule that imposes on a payor that obligation has absolutely no statutory authority and is unenforceable. The information required in the I.F. rule of the payor is too broad and can't all be used. Chevron suggest MMS completely delete Section 210.55 from the I.F. rule. This section is too burdensome on the payor to provide information. All MMS can really do is impose on lessees.
- Lessee won't know Revenue Source (for AID number) so it's not fair to require that of them; get that after MMS receives designation. Revenue source is between payor and MMS (if I designate you to pay, you file PIF).
- Remove the percentage of ownership requirement (218.44); it's too burdensome. Also remove 218.52 pt. 4 (10) - copy of written designation. You're getting the designation, why also say this? Believe 210.55 is illegal (illegal to write in a rule, but we'll give you the information when you ask during audit). Let's go back to the table and figure out designation.

Ken V. - I don't remember why we put the percentage of ownership into the lessee requirements. It shouldn't be mandatory. We only need the right to ask; some people in MMS believe we need the percentage of ownership for other reasons (entitlements).

Don Sant - We will probably remove "copy of designation."

Don Lynch - The general intent of the Interim Final rule is the same as we came up with last fall.

John Clark - At meetings, we generally agreed that payors were the best starting point. I don't disagree. But, there are payors who would be burdened with doing that and for those payors MMS needs to find ways to get information a different way (Example: Companies with systems built around agreements vs. Leases).

George B. - You don't have authority to ask for designations for periods before 9/96.

Ken V. - FOGRMA required designations since 1982.

George B. - What about Section 210. Are you going to have a new form for payors (like the new form MMS created for designations)?

Ken Vogel - We want the authority to ask. We agree with you that on a fundamental basis, lessees are primarily liable. We are not in any way fixed in how we plan to collect the data. We have an obligation to the lessees to make at least the first attempt as easy as possible to do. We need to know who the lessees are and what their relationship is to MMS and the payors.

Don S. - We can't just identify lessees and expect them to file designations that relates to our accounting system. Payors have information that relates to our accounting system. We would like to depend on lessees to file designations.

Ken Vogel - Part of what we're doing now is getting lessees to designate payors. Unfortunately it's a painful process. A lot of lessees don't understand the relationship with the lessor. There are fewer payors than lessees. So it's easier to start with payors. I don't expect to come after payors on a continual basis.

John Clark - We don't know what the intent is on payors.

Patsy Bragg - I think that's the disconnect. If payors think MMS might ask again for an effort like the January D.P. letter, they might make different decisions. Decisions made on how much to spend to get the information would be based on different criteria than if this was a one-shot deal.

Don Sant - I don't foresee a massive D.P. letter again. But if a year from now we don't get the designations, we might do that and place some burden on payors again.

Ken Vogel - I can't tell you to what extent auditors will ask you for the data.

John Clark - For payors where this creates a great burden, will MMS work with them.

Ken Vogel - We will gladly take assumption of liability from payors in lieu of having to provide this information.

Don Sant - If payors don't comply, MMS will move forward on compliance.

Ken Vogel - But we would first call payors and try to work out a plan.

Stranger Payments

George Butler - What is MMS going to do with stranger payments (payments made by someone not lessee or designee): accept and disburse; address through penalties; or reject. I suggest MMS accept so can fulfill responsibilities.

Don S. - At this point, MMS would not even know whether a payment was a "stranger payment."

August 14 Dear Payor Letter

Patsy B. - Considering the burden attached to the January and 8/14 letters for the payors that do not have direct access to the information you need, doesn't it make sense at this point to go directly to the lessees?

Don S. - Are you objecting to the 8/14 letter? Amoco says yes. George B. Says no. Even if we go to lessees, it will at least put them on notice that they are required by RSFA. We need the accounting information that ONLY payors have so we can tie the lessee information to the payor records.

Don Lynch - Lots of them are Mom & Pops. MMS has no idea who they are. Moms and Pops don't know they need to designate or who is paying. MMS said the only people who know anything at all is the payors.

George B. - Do you think lessees will have no clue? Do you believe that?

John Clark et. al. - George, many of the lessees have no idea who is paying royalty. Example: Purchaser (MMS payor) pays operator and MMS but does not know to whom operator disburses (owners). Owners don't know who's paying royalty. Payors and owners don't know each other.

Don Sant & Ken Vogel - We plan to enforce the D.P. letter if people fail to voluntarily comply. However, we will do what we can to help people comply if they let us know they are having trouble.

Patsy Bragg - Have you had any challenges to 8/14 letter? Any affirmative responses?
Larry Gratz - No challenges. Some have responded already.

Patsy Bragg - Asked about the anonymous letter that was circulated to members of Congress challenging the 8/14 letter.
MMS people hadn't heard of this letter.

Takes vs. Entitlements Issue

Don Sant - Are you a designee by paying more than your working interest ownership?

Don Lynch - We say no. But I'm concerned about liability. It complicates designation if you have a different answer.

Don S. - To the extent paying on takes, the rule is likely to say you report to your lease.

Ken W. - 8(g) leases, that won't apply.

Lessee of Record AND Operating Rights Designations

Ken Vogel - Yes, we want Lessee of Record AND Operating Rights designations.

George Butler - Change your mind!

Don Sant - I differ here. I don't want designations from "naked lessees"

Ken V. - Lessees of Record are secondarily liable.

Process in the Future

Bill Strain created a flow chart (see attached) that the group discussed. The group seemed to agree with the flow: 1) Go to designee database, then 2) to BLM or MMS Offshore (if necessary), and 3) only go to payors on an exception basis, if unable to get information from (1) or (2).

Ken Vogel - In most cases we'll have enough information in the designee database to go straight to demand.

George Butler - I'm surprised you think you need to educate lessees.

Don Sant - For the same reason we do payor training.

George B. - Because it's in YOUR interest.

Ken Vogel & Don Sant - Educating lessees would be in YOUR interest too.

MMS Goals:

- 1) To encourage Lessees to file designations
- 2) To be able to timely issue demands with notice to lessees who have designated
- 3) To minimize costs
- 4) To maximize collections

TTTT LEASE NO:
TTTT LEASE NAME:
TTTT OWNER NO:
FEDERAL AID NO:

Lessee of the Federal and/or OCSLA leases, shown above, hereby designates Texaco Trading and Transportation, Inc. as its "designee" pursuant to 30 U.S.C. Sec. 1712 for purposes of the payment of royalty on the oil produced from said leases from the date Texaco first began purchasing.

AGREED AND ACCEPTED BY:

TEXACO TRADING AND TRANSPORTATION INC.

LESSEE:

BY: _____

Sr. Vice Pres. Finance & Admin.

Date: _____

Address: _____

By: _____

Title: _____

Date: _____

Address: _____

DESIGNATION FORM

SUBMIT ONE FORM PER REVENUE SOURCE CODE - INSTRUCTIONS ON REVERSE SIDE

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9/4/97

MMS/Industry Meeting

